(1) Supreme Court, U.S.
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No. 99-

IN THE

Supreme Court of the United States

LOCAL 1199J,

Petitioner,

v.

OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF UNITED HEALTH CARE SYSTEM, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the United Health Care System, Inc. (the "Debtor" or "United") was an "employer" within the meaning of the Worker Adjustment and Retraining Notification Act ("WARN Act"), 29 U.S.C. § 2101, *et seq.*, when it employed 1,300 employees for sixteen (16) consecutive days after filing its Chapter 11 bankruptcy petition, in order to care for over 160 patients, to assist in the orderly transition of those patients to Saint Barnabas Health Care System ("St. Barnabas"), to catalog and inventory assets, and to perform other essential functions as a Chapter 11 debtor-in possession.

2. Whether the United States Court of Appeals for the Third Circuit incorrectly decided that United was not operating as a going concern under the WARN Act, but rather as a business liquidating its affairs, not subject to the WARN Act notification requirements, thereby not requiring the payment of 60 day's pay and benefits.

3. Whether the United States Court of Appeals for the Third Circuit incorrectly found that "employer" status under the WARN Act is not dependent on whether employees continue to work on a daily bases, after a filing a Chapter 11 Bankruptcy petition, but rather whether the employer performs pre-Chapter 11 work.

4. Whether the United States Court of Appeals for the Third Circuit incorrectly created an exception for a Chapter 11 Bankruptcy filing that is not found in the WARN Act, as the only enumerated two exemptions are for "faltering companies" and "unforeseeable business circumstances."

LIST OF PARTIES

United Health Care System, Inc., Medical Staff of United Healthcare System, Inc., DAIWA, and JENSO, District Council I were appellees before the Third Circuit Court of Appeals and are being served as respondents herein.

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The petitioner, Local 1199J respectively petitions this Honorable Court to issue a Writ of Certiorari to review the December 29, 1999 Order of the United States Court of Appeals for the Third Circuit reversing the United States District Court for the District of New Jersey and finding that the WARN Act claim of the United employees should be dismissed.

OPINIONS BELOW

The opinion of the United States Bankruptcy Court is appended hereto as Exhibit C. The opinion of the United States District Court for the District of New Jersey is appended hereto as Exhibit B. The opinion of the United States Court of Appeals for the Third Circuit is appended hereto as Exhibit A. These decisions are unpublished to the petitioner's knowledge.

STATEMENT OF JURISDICTION

On December 29, 1999 the United States Court of Appeals for the Third Circuit reversed the decision of the United States District Court for the District of New Jersey and dismissed the WARN Act claim of the former employees of United. This Petition for Writ of Certiorari was filed within ninety (90) days of the December 29, 1999 decision of the Third Circuit Court of Appeals. This Court's jurisdiction is invoked pursuant to 28 U.S.C. § 1254.

STATUTORY PROVISIONS INVOLVED

The WARN Act, 29 U.S.C. § 2101, *et seq.*, provides in pertinent part as follows:

(a) Definitions

As used in this chapter

(1) the term "employer" means any business enterprise that employs

(A) 100 or more employees, excluding part-time employees; or

(B) 100 or more employees who in the aggregate work at least 4,000 hours per week (exclusive of hours of overtime);

(2) the term "plant closing" means the permanent or temporary shutdown of a single site of employment, or one or more facilities or operating units within a single site of employment, if the shutdown results in an employment loss at the single site of employment during any 30-day period for 50 or more employees excluding any part-time employees;

(3) the term "mass layoff" means a reduction in force which

(A) is not the result of a plant closing; and

(B) results in an employment loss at the single site of employment during any 30 day period for

(i)(I) at least 33 percent of the employees (excluding any part-time employees); and

(II) at least 50 employees (excluding any part-time employees); or

(ii) at least 500 employees (excluding any part-time employees);

(4) the term "representative" means an exclusive representative of employees within the meaning of section 159(a) or 158(f) of this title or section 152 of Title 45;

(5) the term "affected employees" means employees who may reasonably be expected to experience an employment loss as a consequence of a proposed plant closing or mass layoff by their employer;

(6) subject to subsection (b) of this section, the term "employment loss" means (A) an employment termination, other than a discharge for cause, voluntary departure, or retirement, (b) a layoff exceeding 6 months, or (c) a reduction in hours of work of more than 50 percent during each month of any 6-month period;

(7) the term "unit of local government" means any general purpose political subdivision of a State which has the power to levy taxes and spend funds, as well as general corporate and police powers; and

(8) the term "part-time employee" means an employee who is employed for an average of fewer than 20 hours per week or who has been employed for fewer than 6 of the 12 months preceding the date on which notice is required.

(b) Exclusions from definition of employment loss

(1) In the case of a sale of part or all of an employer's business, the seller shall be responsible for providing notice for any plant closing or mass layoff in accordance with section 2102 of this title, up to and including the effective date of the sale. After the effective date of the sale of part or all of an employer's business the purchaser shall be responsible for providing notice for any plant closing or mass layoff in accordance with section 2102 of this title. Notwithstanding any other provision of this chapter, any person who is an employee of the seller (other than a part-time employee) as of the effective date of the sale shall be considered an employee of the purchaser immediately after the effective date of the sale

(2) Notwithstanding subsection (a)(6) of this section, an employee may not be considered to have experienced an employment loss if the closing or layoff is the result of the relocation or consolidation of part or all of the employer's business and, prior to the closing or layoff

(A) the employer offers to transfer the employee to a different site of employment within a reasonable commuting distance with no more than a 6-month break in employment; or

(B) the employer offers to transfer the employee to any other site of employment regardless of distance with no more than a 6-month break in employment, and the employee accepts within 30 days of the offer or of the closing or layoff, whichever is later.

Notice required before plant closing and mass layoffs

(a) Notice to employees, State dislocated worker units, and local governments

An employer shall not order a plant closing or mass layoff until the end of a 60 day period after the employer serves written notice of such an order

(1) to each representative of the affected employees as of the time of the notice or, if there is no such representative at that time, to each affected employee; and

(2) to the State dislocated worker unit (designated or created under title III of the Job Training Partnership Act [29 U.S.C.A. § 1651 et seq.]) and the chief elected official of the unit of local government which the employer shall notify is the unit of local government to which the employer pays the highest taxes for the year preceding the year for which the determination is made.

(b) Reduction of notification period

(1) An employer may order the shutdown of a single site of employment before the conclusion of the 60-day period if as of the time that notice would have been required the employer was actively seeking capital or business which, if obtained, would have enabled the employer to avoid or postpone the shutdown and the employer reasonably and in good faith believed that giving the notice required would have precluded the employer from obtaining the needed capital or business.

(2)(A) An employer may order a plant closing or mass layoff before the conclusion of the 60-day period if the closing or mass layoff is caused by business circumstances that were not reasonably foreseeable as of the time that notice would have been required.

(B) No notice under this chapter shall be required if the plant closing or mass layoff is due to any form of natural disaster, such as flood, earthquake, or the drought currently ravaging the farmlands of the United States.

(3) An employer relying on this subsection shall give as much notice as if practicable and at that time shall give a brief statement of the basis for reducing the notification period.

(c) Extension of layoff period.

A layoff of more than 6 months which, at its outset, was announced to be a layoff of 6 months or less, shall be treated as an employment loss under this chapter unless

(1) the extension beyond 6 months is caused by business circumstances (including unforeseeable changes in price or cost) not reasonably foreseeable at the time of the initial layoff; and

(2) notice is given at the time it becomes reasonably foreseeable that the extension beyond 6 months will be required.

(d) Determinations with respect to employment loss

For purposes of this section, in determining whether a plant closing or mass layoff has occurred or will occur, employment losses for 2 or more groups at a single site of employment, each of which is less than the minimum number of employees specified in section 2101(a)(2) or (3) of this title but which in the aggregate exceed that minimum number, and which occur within any 90-day period shall be considered to be a plant closing or mass layoff unless the employer demonstrates that the employment losses are the result of separate and distinct actions and causes and are not an attempt by the employer to evade the requirements of this chapter.

§ 2103. Exemptions

This chapter shall not apply to a plant closing or mass layoff if

(1) the closing is of a temporary facility or the closing or the layoff is the result of the completion of a particular project or undertaking, and the affected employees were hired with the understanding that their employment was limited to the duration of the facility or the project or undertaking; or

(2) the closing or layoff constitutes a strike or constitutes a lockout not intended to evade the requirements of this chapter. Nothing in this chapter shall require an employer to serve written notice pursuant to Section 2102(a) of this title when permanently replacing a person who is deemed to be an economic striker under the National Labor Relations Act [29 U.S.C.A. § 151, *et seq.*]: Provided,

> that nothing in this chapter shall be deemed to validate or invalidate any judicial or administrative ruling relating to the hiring of permanent replacements for economic strikers under the National Labor Relations Act.

STATEMENT OF THE CASE

The District Court correctly adopted the ruling the Bankruptcy Court that United, is an "employer," and is subject to the WARN Act. United provided a Termination Notice to its 1,300 employees on February 19, 1997, shortly after the Chapter 11 filing. United continued the post-petition employment of its workers for sixteen (16) days. This continued employment was essential for United to conclude the sale which resulted in the receipt of over $13 million, and led to the protection of the health and safety of United's patients. Because United is a fiduciary that continued to operate its business for the benefit of patients as well as creditors, it is subject to the WARN Act's regulations. The District Court properly gave deference to the business judgment of the Debtor's Board of Trustees, in following the reasoning of the Bankruptcy Court.

The Bankruptcy Court also properly refused to apply the "faltering company" and "unforeseeable business circumstances" exemptions from the WARN Act. These are the only exceptions that are found in the WARN Act; the Court of Appeals incorrectly created a third exception for a debtor-in-possession in a Chapter 11 bankruptcy action, an exception not found in the WARN Act. The Bankruptcy Court correctly found, based upon the testimony and evidence, that the financial difficulties that eventually led to United's closure of its facilities were long-term, dire and well known to the United Board and senior management. The Bankruptcy Court also found that the Debtor was not seeking capital, financing or business as a long-term solution for survival. Rather, since the middle of 1996, United knew it could only survive if it could find a merger

partner or purchaser. The ultimate termination of United's employee's certainly was neither unforeseen nor the result of unforeseen circumstances.

The Circuit Court improperly went beyond the clear language of the WARN Act by creating a new exception not contained in the WARN Act. If a bankruptcy employer operates on a daily basis, no matter what its objective, it continues to operate, and its workers continue to be protected by the WARN Act.

REASONS FOR GRANTING THE WRIT

I.

THE BANKRUPTCY COURT AND DISTRICT COURT CORRECTLY HELD THAT UNITED CONTINUED AS AN "EMPLOYER" AFTER THE CHAPTER 11 FILING AND WAS SUBJECT TO THE PROVISIONS OF THE WARN ACT.

The Department of Labor's comments to the WARN Act's regulations make specific reference to the WARN Act's application to companies in bankruptcy:

> [A] fiduciary whose sole function in the bankruptcy process is to liquidate a failed business for the benefit of creditors does not succeed to the notice obligations of the former employer because the fiduciary is not operating a "business enterprise" in the normal commercial sense. In other situations, where the fiduciary may continue to operate the business for the benefit of creditors, the fiduciary would succeed to the WARN obligations of the employer precisely because the fiduciary continues the business in operation.

54 Fed. Reg. 16042, 16045 (1989). The clear implication of these comments is that if a fiduciary continues to operate the

business for the benefit of creditors, it will be required to give notice under the WARN Act. *See In re Hanlin Group, Inc.*, 176 B.R. 329, 332 (Bankr. D.N.J. 1995) (Chapter 11 debtor is subject to WARN requirements where it kept a plant in operation for at least one month after Chapter 11 petition was filed).

As the Bankruptcy Court noted, United, the debtor-in-possession, continued to operate its business by employing 1,300 employees for sixteen (16) days after the Chapter 11 petition was filed. United continued to operate its business for the benefit of existing patients, creditors, and all other parties in interest, including its employees. Thus, the Bankruptcy Court and District Court correctly held that United is subject to the provisions of the WARN Act.

The Circuit Court improperly created a new exception to the WARN Act when it ruled:

> In light of the Department of Labor commentary to the regulations and the cases cited, we believe that whether a bankruptcy entity is an "employer" under the WARN Act depends on the nature and extent of the entity's business and commercial activities while in bankruptcy, and not merely on whether the entity's employees continue to work "on a daily basis." The more closely the entity's activities resemble those of a business operating as a going concern, the more likely it is that the entity is an "employer;" the more closely the activities resemble those of a business winding its up its affairs, the more likely it is the entity is not subject to the WARN Act.
>
> Based upon our review of the Bankruptcy's Court's findings of fact, we find that United Healthcare, as the fiduciary in bankruptcy proceedings, was operating not as a "business operating as a going concern," but rather as a business liquidating its affairs. On February 18, 1997, United Healthcare

surrendered its certificates of need; on February 19, it filed a voluntary bankruptcy plan under which it would liquidate its assets and cease to exist; and, no later than February 21, United Healthcare had discharged or transferred all of its patients and was no longer admitting new patients. Significantly, after February 19, but in any event no later than February 21, its employees were no longer engaged in their regular duties but instead were performing task solely designed to prepare United Healthcare for liquidation.

We recognize that United Healthcare filed for Chapter 11 bankruptcy, ordinarily used to reorganize, rather than Chapter 7 bankruptcy, generally used to liquidate. But as discussed, United Healthcare's actions from the time it filed its Chapter 11 petition throughout the proceedings clearly demonstrate its intent to liquidate. Simultaneously, United Healthcare filed for bankruptcy, agreed to sell its assets and goodwill to St. Barnabas, and surrendered its certificates of need. Had United Healthcare's conduct and activities demonstrated a bona fide effort toward reorganization, the evidence may have shown that United Healthcare was an "employer" subject to the WARN Act.

. . . . In this case, there is no evidence United Healthcare knew in advance that it would be forced to close but concealed that knowledge from its employees. Instead, the record demonstrates that United Healthcare made repeated and intensive good-faith efforts to remain financially viable and to ensure its employees would keep their jobs. Furthermore, United Healthcare willingly disclosed its financial difficulties to its employees, including them in its efforts to find a merger partner. Clearly, United Healthcare did not file for bankruptcy in an effort to avoid its WARN Act responsibilities.

United did not file for bankruptcy in an effort to avoid its WARN Act responsibilities, because as an ongoing concern after it filed for bankruptcy, it understood that it had to comply with the WARN Act requirements.

A. United, as a Chapter 11 Debtor, is Subject to the WARN'S Act's Notice Requirements.

The Third Circuit failed to address language within the commentary of the Department of Labor which answers the question of whether a Chapter 11 debtor-in-possession is an "employer" under the WARN Act. That language indicates that the Department of Labor intentionally chose not to carve out an exception for bankruptcy fiduciaries from the WARN Act requirements. The commentary states that "another commentator suggested that fiduciaries in bankruptcy proceedings should be excluded from the definition of employer. . . . Because adequate protections for fiduciaries are available through the bankruptcy courts, the Department does not think it appropriate to change the regulations to address this situation." 54 Fed. Reg. 16042, 16045 (1989). Accordingly, the Department of Labor did not intend to create an exemption from the WARN Act requirements for bankruptcy fiduciaries beyond those available in the bankruptcy courts.

United, as debtor-in-possession, continued to be an employer subject to the notice requirements of the WARN Act after the Chapter 11 filing. In analyzing the language of the Federal Register, which is merely the Department of Labor's acknowledgment of the protections afforded by the bankruptcy courts, it is apparent that the first sentence of the Department of Labor's comments contemplates a Chapter 7 bankruptcy, while the second sentence contemplates a Chapter 11 bankruptcy. (*See* 54 Fed. Reg. 16042, 16045, *supra*.)

When a debtor files under Chapter 7 of the Bankruptcy Code, the business and any available assets are sold and the creditors are paid from the liquidated proceeds. Under Chapter 11, however, the business may continue to operate while it undergoes a reorganization. Where, as here, the Debtor's business continued to employ 1,300 employees, the fiduciary is liable under WARN because it continued the business operation. The Bankruptcy Court noted this difference when it held that, "[i]n the Chapter 11 context, however, the debtor-in-possession ("DIP") as fiduciary succeeded to the WARN obligations of United under the second scenario outlined by the Department of Labor comment emphasized above . . ." The District Court after reviewing the record below correctly affirmed the Bankruptcy Court's findings in full. The Court of Appeals, though, created an unanticipated exception for a Chapter 11 filing.

B. United is an Employer Subject to the WARN Act's Notice Requirements.

The WARN Act defines the term "employer" to include any "business enterprise which employs: (A) 100 or more employees, excluding part-time employees; or (B) 100 or more employees who aggregate work at least 4,000 hours per week (exclusive of hours of overtime)." 29 U.S.C. § 2101(a). United was, without question, a business enterprise. By employing 1,300 employees on a daily basis for sixteen (16) days after the Chapter 11 filing, United met the minimum threshold of 100 employees set forth in 29 U.S.C. § 2101(a). After the Chapter 11 was filed, United continued to employ these 1,300 individuals. The employees worked far more than an aggregate of 4,000 hours per week. Therefore, United was an employer subject to the requirements of the WARN Act.

The Third Circuit ruled that notwithstanding United's employment of 1,300 individuals to continue the care of over 160 patients, assist in the orderly transition of those patients to

SBHCS, catalog inventory and assets and perform other essential functions, United did not qualify as a business enterprise within the meaning of 29 U.S.C. § 2101(a). The Third Circuit cites *Adams v. Erwin Weller Co.*, 87 F.3d 269, 272-73 (8th Cir. 1996) and *Chauffeurs, Sales Drivers, Warehousemen & Helpers Union Local 572, International Brotherhood of Teamsters, AFL-CIO v. Weslock Corp.*, 66 F.3d 241, 244 (9th Cir. 1995), as support for this proposition. Both of these cases, as well as the additional cases cited by the Committee, are easily distinguished and fail to support the Third Circuit's conclusions.

In *Adams*, a secured lender took possession of the debtor's plant after the debtor had already closed the plant. The secured creditor never reopened the plant for business. In holding that the secured lender was not subject to the WARN'S Act's notice requirements, the Eighth Circuit specifically noted that the secured lender "never assumed an employer-employee relationship by hiring, firing, paying, or supervising any of [the debtor's] employees." *Adams*, 87 F.3d at 273. In contrast, United, as a debtor-in-possession after the Chapter 11 filing, continued to maintain an employer-employee relationship with over 1,300 employees that it paid, supervised and over whom it had the authority to terminate. Pursuant to the reasoning of the Eighth Circuit in *Adams*, United was an employer subject to the WARN Act.

Similarly, in *Chauffeurs*, the court also held that a secured creditor was not subject to the WARN Act's notice requirements, where the creditor's interaction with the debtor was primarily limited to financial controls to preserve its security interest. *Chauffeurs*, 66 F.3d at 245. *Chauffeurs* is distinguishable from the facts here because United had direct control over the business and maintained an employer-employee relationship with its employees, while the secured creditor in *Chauffeurs* simply possessed financial controls. The reasoning of *Chauffeurs* is simply inapplicable to the facts here.

The Supreme Court should accept the District Court's determination that United is an employer subject to the provisions of the WARN Act, because it continued to employ 1,300 employees on a daily basis for 16 days after the Chapter 11 filing. *See Hanlin*, 176 B.R. at 332 (court finding that the debtor was subject to the WARN Act because it "kept the plant in operation for at least one month after the petition was filed, and continued to operate the business as a whole for the benefit of all parties in interest"). By continuing to employ these individuals, United was operating the business for its patients, the estate, creditors and all parties in interest. It was then subject to the WARN Act's notice requirements.

II.

THE BANKRUPTCY COURT AND DISTRICT COURT CORRECTLY HELD THAT THE "FALTERING COMPANY" EXEMPTION FROM THE WARN ACT DOES NOT APPLY.

The "faltering company" exemption from the WARN Act provides as follows:

> An employer may order the shutdown of single site of employment before the conclusion of the 60-day period if as of the time that notice would have been required the employer was *actively seeking capital or business which, if obtained, would have enabled the employer to avoid or postpone the shutdown and* the employer reasonably and in good faith believed that *giving the notice required would have precluded the employer from obtaining the needed capital or business.*

29 U.S.C. § 2102(b)(1) (emphasis added).

The "faltering company" exemption is to be narrowly construed, and only applies when the plant closing results from the employer's failure to obtain sufficient capital, financing or business to continue its operations. *Carpenters Dist. Council v. Dillard Dept. Stores*, 15 F.3d 1275, 1281 (5th Cir. 1994), *cert. denied*, 513 U.S. 1126 (1995); 54 Fed Reg. 16061.

The Department of Labor Regulations identify the four stringent requirements necessary for the "faltering company" exemption to apply:

> (a) The exception under section (2102(b)(1)) of WARN, termed "faltering company", applies to plant closings but not to mass layoffs and should be *narrowly construed*., To qualify for reduced notice under this exception:
>
> (1) An employer must have been *actively seeking capital or business at the time that 60-day notice would have been required.* That is, the employer must have been seeking *financing or refinancing* through the arrangement of loans, the issuance of stocks, bonds, or other methods of internally generated financing; or the employer must have been seeking *additional money, credit, or business* through any other commercially reasonable method. The *employer must be able to identify specific actions taken* to obtain capital or business.
>
> (2) There must have been a *realistic opportunity to obtain the financing* or the business sought.
>
> (3) The financing or business sought must have been sufficient, if obtained, to have enabled the employer to *avoid or postpone the shutdown* . . . for a reasonable period of time.

> (4) The employer reasonably and in good faith must have believed that giving the required notice would have precluded the employer from obtaining the needed capital or business.

20 C.F.R. § 639.9 (1997) (emphasis added).

To qualify for the "faltering company" exemption, it must be demonstrated that *all four* conditions have been met. *United Paperworkers Int'l Union v. Alden Corrugated Container Corp.*, 901 F. Supp. 426, 441 (D. Mass. 1995).

To avoid the 60-day notice requirement under the "faltering company" exemption, the employer must show that it was seeking capital which would have enabled the plant closing to be avoided or postponed. *Carpenters Dist. Council v. Dillard Dept. Stores, supra.* It is not enough that the employer was merely seeking capital, but that obtaining the capital also would have "delayed or avoided the plant closings." *Id.* at 306.

As demonstrated below, the "faltering company" exemption is inapplicable because United was not seeking capital at all, much less to avoid or delay the closing of the facility. Rather, United was merely seeking either to merge with another entity or to negotiate the sale of assets to a purchaser.

The Bankruptcy Court heard uncontroverted evidence that as of the Fall of 1996, United was seeking to either merge or sell its operations. United had abandoned its attempts to obtain long-term conventional financing, and merely sought interim financing (with Daiwa) pending consummation of a sale or merger.

Courts have specifically held that the "faltering company" exemption does not apply to companies that are *merging* or trying to *sell* their assets, as United was here. The Fifth Circuit, for example, refused to apply the "faltering company" exemption to a merger situation, holding that the exemption "applies only

when a layoff is caused by the employer's failure to obtain sufficient *capital*." *Carpenters Dist. Council*, 15 F.3d at 1281 (emphasis added). The court held that the exemption is inapplicable because the cause of the layoff is the merger of two companies, not the failure to obtain capital. *Id.*

Similarly, trying to sell a plant is not considered "actively seeking capital or business" and is therefore *not* covered by the "faltering company" exemption. *See Wallace v. Detroit Coke Corp.*, 818 F. Supp. 192, 197 (E.D. Mich. 1993); *Local 397, Int'l Union of Electronic Machine & Furniture Workers v. Midwest Fasteners, Inc.*, 763 F. Supp. 78, 83-84 (D.N.J. 1990); *but see United Paperworkers*, 901 F. Supp. at 441 (attempts to sell company is a factor in analysis of "faltering company").

United was engaged in an effort to sell its assets to potential purchasers, including the ultimate successful bidder, St. Barnabas, and therefore could not qualify for the "faltering company" exemption under the WARN Act. In December of 1996, United was in exclusive negotiation with St. Barnabas to sell its assets. (Bankruptcy Court Opinion at p. 12). It was not "actively seeking capital or business which, if obtained, would have enabled the employer to avoid or postpone the shutdown." 29 U.S.C. § 2102(b)(1); 20 C.F.R. § 639.9(b)(1),(2). Clearly, United was not seeking to "avoid or postpone the shutdown." 20 C.F.R. § 639.9(a)(3). Rather, these negotiations to sell its assets resulted in the ultimate shutdown of the hospital.

Finally, United could not have "reasonably . . . believed that giving the required notice would have precluded [it] from obtaining the needed capital or business." *Id.* at (a)(4). Because United could not establish that *any one* of the conditions in the Regulations have been met, much less *all four* as required, it could not qualify for the "faltering company" exemption under the WARN Act.

III.

THE BANKRUPTCY COURT AND DISTRICT COURT CORRECTLY FOUND THAT THE "UNFORESEEABLE BUSINESS CIRCUMSTANCES" EXEMPTION DOES NOT APPLY.

The "unforeseeable business circumstances" exemption from the WARN Act provides that "[a]n employer may order a plant closing or mass layoff if caused by business circumstances that were not reasonably foreseeable as of the time that notice would have been required." 29 U.S.C. § 2102(b)(2)(A). The unforeseeable business circumstances exemption from the WARN Act is also to be narrowly construed. *Carpenters Dist. Council v. Dillard Dept. Stores, Inc., supra,* 15 F.3d at 1282. In further defining and clarifying this exception, the regulations provide, in relevant part:

> *An important indicator of a business circumstance that is not reasonably foreseeable is that the circumstance is caused by some sudden, dramatic, unexpected action or condition and outside the employer's control. . . .* The test for determining when circumstances are not reasonably foreseeable focuses on an employer's business judgment. The employer must exercise such commercially reasonable business judgment as would a similarly situated employer office in predicting the demands of its particular market.

20 C.F.R. §§ 639.9(b)(1), (2) (1977) (emphasis added).

The District Court concluded, after reviewing *de novo* the undisputed facts before the Bankruptcy Court, that the unforeseeable business circumstances exemption does to apply to United. The Bankruptcy Court recited the following facts:

> There were months of warning signals to the Board that placed them on notice that United was in financial extremis and that the facts leading to United filing for bankruptcy on February 19, 1997 were far from an unforeseeable business circumstance so as to justify an exception to the WARN Act.

Consistent with the District Court's and Bankruptcy Court's holding, the unforeseeable business circumstances exemption has been held not to apply where the employer is aware of its financial difficulties during the period leading up to the plant closing or mass layoff. *United Paperworkers Int'l Union v. Alden Corrugated Container Corp.*, 901 F. Supp. 426, 443 (D. Mass 1995) (finding cessation of operations could not be viewed as an unforeseen business circumstances based upon deepening downward fiscal spiral of companies); *In re Riker Indus., Inc.*, 151 B.R. 823, 827 (Bankr. N.D. Ohio 1993) (finding withdrawal of financing should have been anticipated by debtor where it was clearly aware of its precarious financial condition); *Parsley v. Kunja Knitting Mills, U.S.A. Inc.*, No. Civ. A.4:91:0966-15, 1991 WL 340563, at *6 (D.S.C. April 25, 1991) (granting preliminary injunction based upon finding that unforeseeable business circumstances exemption was unlikely to succeed because of arrest of company officials, ongoing customs investigation and persistent legal trouble). *See also Carpenters Dist. Council, supra*, (finding merger and layoff did not constitute unforeseen business circumstance despite uncertainty over whether SEC and stockholders would approve merger). Where an employer is aware of its financial difficulties and can reasonably anticipate a plant closing, the unforeseen circumstance exception simply will not apply when the employer ceases operations.

In a case very similar to the facts here, *Carpenters District Council*, *supra*, the Fifth Circuit held that the fact that there were some uncertainties related to negotiations for a merger did not mean that the resulting merger was unforeseeable. In that case, the defendant corporation had been negotiating for several months with another corporation to reach an agreement allowing the two companies to merge. Those negotiations took place several months before the termination notice should have been given to employees. In fact, a tentative agreement was reached, both companies sought the approval of the Securities and Exchange Commission and the parties began actively promoting the merger. The defendant argued that there was uncertainty as to when, or even if, the SEC would approve the registration statement, and as to whether the other company's stockholders would approve the merger. The court rejected defendant's contentious regarding the unforeseeability exemption and held that the merger was, in fact, foreseeable.

The *United Paperworkers* case is particularly instructive. The debtors in that case were in the business of corrugated cardboard products and experienced substantial losses and financial difficulties over an extended period of time. Both companies attempted to reverse their difficulties in various ways, including establishing a line of credit and reorganizing. The financial losses and business decisions, however, ultimately resulted in their lender calling their loans and both plants were forced to close. Neither company was able to lure a potential purchaser.

Determining that the unforeseen business circumstance exemption did not apply, the court in *United Paperworkers* noted that the fiscal misfortunes of both companies had been quite apparent due to the ever increasing losses they had been sustaining and the fact that their loans were undergoing a workout process with the lender. In light of these ongoing fiscal difficulties, the court held that the lender's directive to cease operations could not be viewed as an unforeseen business

circumstances. 901 F. Supp. at 443. Rather, the court found the decision to be the culmination of the continuing and worsening financial devastation of the companies. *Id.* The facts here are indistinguishable. As early as April 1996 the Debtor projected a $25 million loss. In August and September 1996 the Board of Trustees recognized that United could not stand alone and time was running out to locate a partner. In March 1996 the Debtor experienced problems maintaining essential supplies such as blood. In the Fall of 1996 United's financial condition became so extreme it ceased paying employee health insurance premiums.

In *In re Riker Industries, Inc., supra*, the United States Bankruptcy Court for the Northern District of Ohio found that the closing of the debtor's plant due to a loss of financing was reasonably foreseeable and refused to apply an exception. 151 B.R. at 827. The court held that the loss of financing should have been anticipated by the debtor as it was clearly aware of its precarious financial condition. *Id.*

The facts here are even more compelling than in the cases cited above. The evidence presented to the Bankruptcy Court established that as early as August 1996, United's deteriorating financial condition required United's Board to take steps to ensure the continued viability of its operations. The options included finding a partner willing to continue operations at United's facilities or selling assets to a third party that would perform United's services at other facilities.

United's Board of Trustees commenced looking for a merger/sale candidate in the Fall of 1996. While the Board was attempting to locate a partner that would continue operating the hospital at the Debtor's facilities in Newark, the Board also engaged in discussions regarding a transfer of the Debtor's operations to other facilities in the surrounding areas. Such a transaction would have lead to the shutdown of the Debtor's operations to other facilities in the surrounding areas.

Given the unrefuted facts, the unforeseeable business circumstances exemption is simply inapplicable. The closure of the hospital and the sale of United's goodwill to St. Barnabas was not an unforeseen circumstance. Similar to the transaction which was contemplated in *Carpenters District Counsel*, the sale to St. Barnabas was being negotiated for an extended period of time. Simply because there were uncertainties as to whether the deal would close, does not mean that the ultimate sale was unforeseen. *Carpenters Dist. Counsel*, 15 F.3d at 1282.

The application of the "unforeseen business circumstance" exemption does not apply here. United did not experience any sudden, dramatic event such as those experienced in the cases discussed above that forced the closure of its facility. United was well aware of its dire financial condition months before it was required to consummate the sale with St. Barnabas and terminate hospital operations. Accordingly, the Bankruptcy Court and District Court correctly ruled that the unforeseeable business circumstance exemption does not apply.

CONCLUSION

It is respectfully submitted that the Supreme Court should grant the Writ of Certiorari in this matter to provide meaningful guidelines to lower courts on the application of the WARN Act to employers who file a Chapter 11 bankruptcy petition and thereafter continue to operate their business as debtors-in-possession. The Circuit Court incorrectly carved out an exception for debtors-in-possession that is not found in the WARN Act. Thus, the Writ should be granted.

Respectfully submitted,

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APPENDIX

APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT DATED AND FILED DECEMBER 29, 1999

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 98-6490

IN RE: UNITED HEALTHCARE SYSTEM, INC.,

Debtor

OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF UNITED HEALTHCARE SYSTEM, INC.,

Appellant

v.

UNITED HEALTHCARE SYSTEM, INC.; MEDICAL STAFF; DAIWA; LOCAL 1199J

On Appeal from the United States District Court
for the District of New Jersey
D.C. Civil Action No. 97-cv-02495
(Honorable Joseph A. Greenaway, Jr.)

Argued July 26, 1999

Before: SCIRICA and STAPLETON, *Circuit Judges*, and SHAPIRO, *District Judge**

(Filed: December 29, 1999)

* * *

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* The Honorable Norma L. Shapiro, United States District Judge for the Eastern District of Pennsylvania, sitting by designation.

Appendix A

OPINION OF THE COURT

SCIRICA, *Circuit Judge.*

This case brought under the Worker Adjustment and Retraining Notification Act (WARN Act), 29 U.S.C. §2101 *et seq.*, arises from the Chapter 11 bankruptcy of United Healthcare System, Inc. The Official Committee of Unsecured Creditors of United Healthcare System, Inc. appeals a judgment that former United Healthcare employees are entitled to WARN Act back pay, and receive first priority administrative status in the bankruptcy proceedings. Because we conclude United Healthcare was no longer an "employer" within the meaning of the WARN Act when it terminated these employees and therefore was not subject to the WARN Act, we will reverse.

I.

United Healthcare System, Inc. was a New Jersey not-for-profit corporation that provided hospital and healthcare services in the Newark area. Since 1993, United Healthcare had experienced financial difficulties. But these problems did not become acute until 1996, when the company suffered substantial operating losses and encountered trouble maintaining essential supplies (such as blood). Attempting to alleviate these problems, United Healthcare entered into partnership negotiations with Children's Hospital of Philadelphia and merger negotiations with Atlantic Health Care System. Nothing came to fruition.

Appendix A

Despite its difficulties, United Healthcare did not believe financial problems would force it to close and in mid-December of 1996, its board of directors unanimously approved a budget for 1997. The budget anticipated losses for the first three months of 1997 but projected positive revenues for the rest of the year and predicted a year-end surplus of $1.2 million. United Healthcare's President and Chief Executive Officer John Dandridge later testified that the budget represented the board's good-faith attempt to forecast United Healthcare's finances for the forthcoming year. Shortly after approving the budget, United Healthcare's board commenced discussions with other potential merger partners or purchasers, retaining Merrill Lynch for assistance and to find additional potential partners.

In early 1997, United Healthcare's financial problems worsened and the company began to divert withholding and other tax payments to meet general operating expenses. On January 15, Primary Healthcare Systems made an offer to purchase United Healthcare and continue United Healthcare's operations in the existing Newark facilities with United Healthcare's employees. Taking into account Primary Healthcare's financial condition as well as the time and money it invested in preparing its offer, United Healthcare President Dandridge concluded Primary Healthcare could successfully complete the proposed purchase and continue United Healthcare's business.

As the parties continued to negotiate over Primary Healthcare's proposal in late January, United Healthcare's secured creditor Daiwa Healthco-2 L.L.C. warned that recent financial reports had caused it to doubt United Healthcare's

financial viability. Responding that a computer error caused the reports to contain incorrect data, United Healthcare assured Daiwa that it would soon complete a transaction allowing United Healthcare's facilities to remain open and its employees to remain on the job. But this response did not allay Daiwa's fears and on February 3 Daiwa suspended funding to United Healthcare. As a result, United Healthcare was unable to meet its operating expenses, closed its emergency room and reduced its number of patients. To alleviate United Healthcare's financial problems and to allow it to increase its number of patients, the State of New Jersey gave United Healthcare an emergency funding advance of $5,000,000. After receipt of the advance, United Healthcare apparently increased its number of patients from 120 to 180. But, at the same time, United Healthcare accelerated its merger discussions and then issued requests for merger or acquisition proposals to several health care providers, four of which responded with proposals.

On February 13, 1997, Daiwa issued United Healthcare a notice of default terminating all financing. As a result, United Healthcare was unable to continue operations and meet daily expenses. Also on February 13, Blue Cross terminated, for non-payment, the health insurance United Healthcare provided its employees.

On Sunday, February 16, United Healthcare's board, management, medical staff, consultants and attorneys heard proposals for merger, joint venture or sale of assets and goodwill from Primary Healthcare Systems, St. Barnabas Corporation and UMDNJ/Cathedral Healthcare System, Inc. St. Barnabas and UMDNJ/Cathedral proposed to purchase

only a portion of United Healthcare's assets and then terminate its operation. Primary Healthcare proposed to continue operating United Healthcare as a going concern and to retain 980 of United Healthcare's approximately 1,300 employees. Although United Healthcare's medical staff voted to accept Primary Healthcare's offer, United Healthcare's board voted to accept St. Barnabas' offer to purchase its assets and to close the hospital.

On February 19, United Healthcare advised the New Jersey Department of Health that it would close and surrendered its certificates of need.[1] On that same day, the Department of Health revoked United Healthcare's certificates of need, and issued new certificates of need to a St. Barnabas affiliate as required for the transfer of United Healthcare's services. Also on February 19, United Healthcare filed a voluntary Chapter 11 bankruptcy petition, and provided its approximately 1,300 employees with 60 days' notice of termination of employment pursuant to the WARN Act.[2] The notice explained that their employment

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1. Under New Jersey law, health care facilities are required to maintain certificates of need issued by the Department of Health. N.J.S.A. 26:2H-7 (West 1999) ("No health care facility shall be constructed or expanded, and no new health care service shall be instituted . . . except upon application for and receipt of a certificate of need . . . .").

2. As is more fully explained, the WARN Act requires an employer to provide employees 60 days' notice of a "plant closing" or "mass layoff." 29 U.S.C. §2102. United Healthcare claims the WARN notice followed the bankruptcy filing; the Bankruptcy Court found the two acts were simultaneous.

would end on April 20 or within fourteen days of that date but stated that they should continue to report to work until United Healthcare closed. United Healthcare also filed an emergency application for the sale of its goodwill to St. Barnabas. Because all of United Healthcare's patients had either been transferred to the St. Barnabas hospital affiliate or sent home by February 21, within 48 hours after United Healthcare issued the WARN notice, its employees were unable to perform their regular duties but instead cleaned, took inventory and prepared the company's assets for sale.

On March 4, the Official Committee of Unsecured Creditors of United Healthcare System, Inc. ("Committee")[3] filed a motion asking the Bankruptcy Court to order United Healthcare to terminate all employees immediately. On March 6, before the court ruled on the Committee's motion, United Healthcare informed 1,200 of its 1,300 employees that they were no longer to report to work. United Healthcare retained 100 employees to secure the plant facility and to maintain necessary equipment.

On March 7, United Healthcare and the Committee stipulated before the Bankruptcy Court that United Healthcare's February 19 WARN Act notice created a "$7.3 million payroll obligation." The parties agreed that United Healthcare's 1,200 furloughed employees were entitled to be paid for the sixteen days they actually worked, amounting to $1.7 million. But the parties could not agree whether the

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3. The Committee represents Unsecured Creditors' interests of approximately $20 million.

employees were entitled to WARN Act "back pay"[4] for the remaining forty-four days, an amount of $5.1 million. United Healthcare asserted that the employees were entitled to WARN Act "back pay" for these forty-four days and were also entitled to first priority administrative claim status in bankruptcy under 11 U.S.C. §§503(b)(1)(A) and 507(a)(1). The Committee responded that the employees were not entitled to WARN Act back pay because United Healthcare ceased to be an "employer" subject to the WARN Act once it surrendered its certificates of need on February 18. In the alternative, it also contended United Healthcare was excused from providing notice under the WARN Act's "faltering

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4. The WARN Act provides:

> (1) Any employer who orders a plant closing or mass layoff in violation of section 2102 of this title shall be liable to each aggrieved employee who suffers an employment loss as a result of such closing or layoff for —
>
> > (A) back pay for each day of violation at a rate of compensation not less than the higher of —
> >
> > > (i) the average regular rate received by such employee during the last 3 years of the employee's employment; or
> >
> > > (ii) the final regular rate received by such employee. . . .

29 U.S.C. §2104(a).

company" and "unforeseeable business circumstances" exceptions. Additionally, the Committee maintained that if United Healthcare's furloughed employees were entitled to "back pay" under the WARN Act, they held only unsecured claims limited to $4,000 per employee under 11 U.S.C. §507(a)(3), rather than first priority administrative claims.

In an order dated March 26, 1997, the Bankruptcy Court rejected the Committee's arguments, holding that United Healthcare's employees were entitled to WARN Act back pay and that their claims should be granted first priority administrative claim status. *In re United Healthcare System, Inc.*, No. 97-21785, slip op. (Bankr. D.N.J. Mar. 26, 1997). The Bankruptcy Court held that United Healthcare remained an "employer" subject to the Act after it filed its bankruptcy petition because it continued to employ its 1,300 person workforce for sixteen days after the Chapter 11 petition was filed. In reaching this conclusion, the court was guided by a Department of Labor WARN Act comment which provides, "where the fiduciary may continue to operate the business for the benefit of creditors, the fiduciary would succeed to the WARN obligations of the employers precisely because the fiduciary continues the business in operation." 54 Fed. Reg. 16042 (1989).

The Bankruptcy Court also concluded the so-called "unforeseeable business circumstances" exception, which excuses an employer from providing WARN notice if closing is not reasonably foreseeable sixty days in advance,[5] did not

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5. 29 U.S.C. §2102(b)(2)(A) sets forth what has come to be known as the "unforeseeable business circumstances exception." It provides:

> An employer may order a plant closing or mass layoff before the conclusion of the 60-day period if the closing

(Cont'd)

excuse United Healthcare from providing notice because it found there were "months of warning signals" that placed the board of directors on notice that "United was in financial extremis." Specifically, the court found United Healthcare had suffered substantial losses and had experienced "chronic" supply problems for more than a year before closing. In addition, the court noted that Daiwa had complained to United Healthcare about the "quality of financial information" since December 1996 and that the New Jersey Department of Health had advanced United Healthcare substantial future payments in January 1997.

The Bankruptcy Court also concluded that United Healthcare was not absolved of its WARN Act obligations by the Act's "faltering business" exception, which permits an employer to withhold notice if it is "actively seeking capital or business" that would allow it to postpone or avoid closing and if it reasonably believed that giving notice would have prevented it from obtaining the capital or business.[6]

(Cont'd)

> or mass layoff is caused by business circumstances that were not reasonably foreseeable as of the time that notice would have been required.

See Hotel Employees and Restaurant Employees Int'l Union Local 54 v. Elsinore Shore Associates, 173 F.3d 175, 184-87 (3d Cir. 1999) for a discussion of the "unforeseeable business circumstances exception."

6. This exception is set forth in 29 U.S.C. §2102(b)(1):

> An employer may order the shutdown of a single site of employment before the conclusion of the 60-day period

(Cont'd)

The court determined the exception did not apply because United Healthcare's "deep, long-term and critical" financial problems prevented it from reasonably believing new capital or business would allow it to remain open.

Finally, the Bankruptcy Court concluded that United Healthcare's employees' WARN Act claims were entitled to first priority administrative status under 11 U.S.C. §§503(b)(1)(A) and 507(a)(1) rather than treatment as unsecured claims for wages because the employees' post-petition services "clearly benefitted the estate" and were therefore "actual, necessary costs and expenses," 11 U.S.C. §503(b)(1)(A), of preserving United Healthcare's bankruptcy estate.

The Committee appealed the Bankruptcy Court's judgment to the District Court, which affirmed. The District Court concluded without explanation that United Healthcare was an employer for "sixteen days after the bankruptcy filing." It also held that neither the faltering business exception nor the unforeseeable business circumstances exception applied because of United Healthcare's "sizable, long-term and critical" financial problems and because "merely refinancing or acquiring new lenders would not

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(Cont'd)

> if as of the time that notice would have been required the employer was actively seeking capital or business which, if obtained, would have enabled the employer to avoid or postpone the shutdown and the employer reasonably believed that giving the notice would have precluded the employer from obtaining the necessary capital or business.

prevent the closing of the hospital." Finally, the Court held the employees' WARN Act claims were entitled to first priority administrative status because the employees had performed "necessary and valuable services."

The Committee has appealed.

II.

The Bankruptcy Court had jurisdiction under 28 U.S.C. §157(b)(2)(B). The District Court had jurisdiction under 28 U.S.C. §158(a). We have jurisdiction under 28 U.S.C. §1291.

III.

We address only the threshold question on appeal: whether the Bankruptcy Court and the District Court correctly concluded United Healthcare continued as an "employer" within the meaning of the WARN Act after filing for Chapter 11 bankruptcy, and was therefore subject to the WARN Act notification requirements when it furloughed its 1,200 employees on March 6, 1997.[7] Although we review a bankruptcy court's findings of historical or narrative fact for clear error, *see Mellon Bank v. Metro Communications, Inc.*, 945 F.2d 635, 642 (3d Cir. 1991), the parties do not dispute the accuracy of the Bankruptcy Court's findings of fact, which were undisturbed by the District Court. Instead, the

7. Because we hold that United Healthcare was not subject to the WARN Act, we need not decide whether the WARN Act's "unforeseeable business circumstances" and "faltering business" exceptions apply or whether the "back pay" claims were entitled to first priority administrative claim status.

parties dispute whether the facts were sufficient to support the Bankruptcy Court's legal conclusion that United Healthcare was an employer under the WARN Act, and had violated the Act's notice provisions when it terminated its employees on March 6, 1997. Because this dispute requires us to review the Bankruptcy Court's " 'choice and interpretation of legal precepts and its application of those precepts to the historical facts,' " we apply plenary review. *See id.* (quoting *Universal Minerals, Inc. v. C.A. Hughes & Co.*, 669 F.2d 98, 101-02 (3d Cir. 1981)).

A.

With certain exceptions, the WARN Act, 29 U.S.C. §2101 *et seq.*, requires an "employer" to provide its employees with sixty days' notice of a "plant closing" or "mass layoff." 29 U.S.C. §2102.[8] If the employer fails to do

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8. The statute defines "plant closing" as

> the permanent or temporary shutdown of a single site of employment, or one or more facilities or operating units within a single site of employment, if the shutdown results in an employment loss at the single site of employment during any 30-day period for 50 or more employees excluding any part-time employees.

29 U.S.C. §2101(a)(2).

The statute defines "mass layoff" as

> a reduction in force which —
>
> (A) is not the result of a plant closing; and

(Cont'd)

so, it may be liable for up to sixty days' back pay. *See* 29 U.S.C. §2104(a).

The Committee contends United Healthcare ceased to be an "employer" under the WARN Act when it surrendered its certificates of need, and filed for bankruptcy on February 19, 1997. From that date forward, the Committee maintains, United Healthcare was no longer a business enterprise operating as a going concern, but rather was a company winding up its affairs and preparing for liquidation. United Healthcare contends that after it filed its bankruptcy petition, it continued as an "employer," operating its business for the benefit of creditors, and was therefore subject to the WARN Act notice requirements.

(Cont'd)

> (B) results in an employment loss at the single site of employment during any 30-day period of
>
> > (i)(I) at least 33 percent of the employees (excluding any part-time employees); and
> >
> > (II) at least 50 employees (excluding any part-time employees); or
> >
> > (ii) at least 500 employees (excluding any part-time employees).

Id. §2101(a)(3).

Appendix A

As with all questions of statutory interpretation, we begin with the language of the statute itself. *See United States ex rel. LaCorte v. SmithKline Beecham Clinical Lab., Inc.*, 149 F.3d 227, 232 (3d Cir. 1998); *In re TMI*, 67 F.3d 1119, 1123 (3d Cir. 1995). The WARN Act defines an "employer" as

> any business enterprise that employs —
>
> (A) 100 or more employees, excluding part-time employees; or
>
> (B) 100 or more employees who in the aggregate work at least 4,000 hours per week (exclusive of hours of overtime) . . . .

29 U.S.C. §2101(a)(1). As another court of appeals has explained, this language is general and not especially helpful in determining whether a particular employer is subject to WARN. *See Adams v. Erwin Weller Co.*, 87 F.3d 269, 271 (8th Cir. 1996) (stating that section 2101(a)(1) "does not tell us what it takes to be an employer subject to WARN"). But it does set forth two requirements: an "employer" must employ a certain number of employees and must also be a "business enterprise," a term the statute does not define. In this case, there is no doubt United Healthcare employed the requisite number of employees. But it is less clear that United Healthcare remained a "business enterprise" after it surrendered its certificates of need, stopped treating patients, and entered bankruptcy to liquidate its assets. Each of those events precluded United Healthcare from performing the everyday business functions of a hospital and health care service. On the other hand, despite those events, United

Healthcare remained a corporation that employed for sixteen days a substantial number of employees to whom it assigned various tasks all related to shutting down its operations. Addressing the facts here in context, we do not believe WARN's plain language resolves whether United Healthcare was an "employer" required to provide sixty days notice prior to its termination of the 1,200 employees.

It is appropriate, therefore, to consider agency regulations and comments as well as the case law. *See Hotel Employees*, 173 F.3d at 181-83 (considering regulations, legislative history, cases and legislative purpose when WARN's plain language did not indicate statute's scope). The Department of Labor's comments to its regulations implementing the WARN Act suggest that whether an entity (bankrupt or otherwise) is an "employer" under the WARN Act depends in part on the nature of the entity's activities.

> [T]he term "employer" includes public and quasi-public entities which *engage in business* (i.e., take part in a commercial or industrial enterprise, supply a service or good on a mercantile basis, or provide independent management of public assets, raising revenue and making desired investments) . . . .

20 C.F.R. §639.3(a)(1)(ii), 54 Fed. Reg. 16042, 16065 (1989) (emphasis added). Thus, in determining whether an entity is an "employer," we will consider whether the entity was "engage[d] in business" during the time prior to the plant closing or mass layoff. Elsewhere, the commentary specifically addresses entities in bankruptcy at the time the closing or layoff occurred:

> [T]he Department does not think it appropriate to [exclude all bankrupt companies from the definition of "employer"]. Further, DOL agrees that a fiduciary whose sole function in the bankruptcy process is to liquidate a failed business for the benefit of creditors does not succeed to the notice obligations of the former employer because the fiduciary is not operating a "business enterprise" in the normal commercial sense. In other situations, where the fiduciary may continue to operate the business for the benefit of creditors, the fiduciary would succeed to the WARN obligations of the employer precisely because the fiduciary continues the business in operation.

54 Fed. Reg. at 16045. Thus, the question for us to resolve is whether United Healthcare, as the debtor-in-possession,[9] was operating as an ongoing business enterprise, or whether it was merely engaged in the liquidation of assets. As discussed in the Department of Labor commentary, merely filing for bankruptcy does not exempt an entity from the WARN Act. Instead, the commentary's focus on the bankruptcy fiduciary's responsibilities indicates that whether a bankrupt entity is an "employer" under the WARN Act depends in part on the nature and extent of the entity's business conduct and activities while in bankruptcy.

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9. United Healthcare, as a debtor-in-possession, is a fiduciary for its estate and for its creditors. *See* 11 U.S.C. §1107(a); *Commodity Futures Trading Comm'n v. Weintraub*, 471 U.S. 343, 355 (1985).

Two courts of appeals have relied upon this comment in determining whether a secured creditor can be an "employer" under the WARN Act. In *Chauffeurs, Sales Drivers, Warehousemen & Helpers Union Local 572 v. Weslock Corp.*, the Court of Appeals for the Ninth Circuit examined the secured creditor's degree of control over the debtor, holding a secured creditor could be an employer if it "operates the debtor's asset as a 'business enterprise' in the 'normal commercial sense.' " 66 F.3d 241, 244 (1995) (quoting 54 Fed. Reg. 16045 (1989)). Drawing on *Chauffeurs*, the Court of Appeals for the Eighth Circuit also focused on the nature and extent of the secured creditor's involvement with the debtor, holding a creditor acquires "employer" status when it "becomes so entangled with its borrower that it has assumed responsibility for the overall management of the borrower's business." *Adams*, 87 F.3d at 272.

The Bankruptcy Court, after reviewing the Department of Labor Commentary, held United Healthcare was subject to the WARN Act notification requirements, finding:

> In this case, there is no doubt that United Healthcare's plant closing and massive layoff of employees would, absent bankruptcy, trigger the notification requirements under WARN. In the Chapter 11 context, however, the debtor-in-possession ("DIP") as fiduciary succeeded to the WARN obligations of United . . . since debtor's 1,300 employees continued to work on a daily basis for sixteen days after the Chapter 11 petition was filed.

We disagree. In light of the Department of Labor commentary to the regulations and the cases cited, we believe that whether a bankrupt entity is an "employer" under the WARN Act depends on the nature and extent of the entity's business and commercial activities while in bankruptcy, and not merely on whether the entity's employees continue to work "on a daily basis." The more closely the entity's activities resemble those of a business operating as a going concern, the more likely it is that the entity is an "employer;" the more closely the activities resemble those of a business winding up its affairs, the more likely it is the entity is not subject to the WARN Act.

Based upon our review of the Bankruptcy Court's findings of fact, we find that United Healthcare, as the fiduciary in bankruptcy proceedings, was operating not as a "business operating as a going concern," but rather as a business liquidating its affairs. On February 18, 1997, United Healthcare surrendered its certificates of need; on February 19, it filed a voluntary bankruptcy plan under which it would liquidate its assets and cease to exist; and, no later than February 21, United Healthcare had discharged or transferred all of its patients and was no longer admitting new patients. Significantly, after February 19, but in any event no later than February 21, its employees were no longer engaged in their regular duties but instead were performing tasks solely designed to prepare United Healthcare for liquidation.

We recognize that United Healthcare filed for Chapter 11 bankruptcy, ordinarily used to reorganize, rather than Chapter 7 bankruptcy, generally used to liquidate. But as discussed, United Healthcare's actions from the time it filed

its Chapter 11 petition throughout the proceedings clearly demonstrate its intent to liquidate. Simultaneously, United Healthcare filed for bankruptcy, agreed to sell its assets and goodwill to St. Barnabas, and surrendered its certificates of need. Had United Healthcare's conduct and activities demonstrated a bona fide effort toward reorganization, the evidence may have shown that United Healthcare was an "employer" subject to the WARN Act.

We believe this analysis is consistent with the legislative purpose behind WARN. In *Hotel Employees*, we stated:

> The WARN Act was adopted in response to the extensive worker dislocation that occurred in the 1970s and 1980s. As companies were merged, acquired, or closed, many employees lost their jobs, often without notice. In some circumstances, the projected closing was concealed from the employees. Congress enacted WARN to protect workers and their families from these situations. WARN's notice period was designed to allow workers "to adjust to the prospective loss of employment, to seek and obtain retraining that will allow [them] to successfully compete in the job market." [20 C.F.R. § 639.1(a)]. The thrust of WARN is to give fair warning in advance of prospective plant closings. It would appear, therefore, that if an employer knew of a .... closing and failed to notify its employees, the WARN Act would apply.

173 F.3d at 182. In this case, there is no evidence United Healthcare knew in advance that it would be forced to close but concealed that knowledge from its employees. Instead, the record demonstrates that United Healthcare made repeated and intensive good-faith efforts to remain financially viable and to ensure its employees would keep their jobs. Furthermore, United Healthcare willingly disclosed its financial difficulties to its employees, including them in its efforts to find a merger partner. Clearly, United Healthcare did not file for bankruptcy in an effort to avoid its WARN Act responsibilities.

Although we find WARN Act liability does not attach under these facts and circumstances, we do not foreclose the possibility that WARN Act liability may apply to other situations where an employer files for bankruptcy and then terminates its employees. An employer as fiduciary will succeed to its WARN Act obligations if an examination of the debtor's economic activities leading up to and during the bankruptcy proceedings reveals that the fiduciary has continued in an "employer" capacity, operating the business as an ongoing concern.

IV.

In conclusion, we do not believe United Healthcare continued as an "employer" within the meaning of the WARN Act when it assumed the role of fiduciary following the filing for bankruptcy. At that time, it ceased operating its business as a going concern and was simply preparing itself for liquidation. The bankruptcy plan it filed simultaneously with its Chapter 11 petition confirms this

assessment: United Healthcare planned to sell its goodwill to St. Barnabas and would itself cease to exist. Given these prospects and the absence of any evidence United Healthcare structured its bankruptcy petition and the furlough of its employees to avoid WARN Act liability, we hold United Healthcare was no longer subject to the WARN Act when it furloughed its employees.[10]

For these reasons, we will reverse the District Court's order of November 5, 1998, to the extent it is inconsistent with this opinion and will remand for proceedings consistent with this opinion.

A True Copy:
Teste:

Clerk of the United States Court of Appeals for the Third Circuit

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10. We express no opinion on whether United incurred WARN liabilities at some point prior to the filing of its petition and whether the United employees have WARN claims entitled to priority under Section 507(a)(3).

APPENDIX B — ORDER OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY DATED AND FILED NOVEMBER 5, 1998

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

Civ. No. 97-2495 (JAG)

In the Matter of:

United Healthcare System, Inc.,

Debtor-in-Possession.

ORDER

This matter having come before the Court by way of appellant Official Committee of Unsecured Creditors of United Healthcare System, Inc.'s ("Appellant") application seeking reversal of the March 26, 1997 Opinion and Order of the United States Bankruptcy Court, District of New Jersey (Tuohey, J.), which held that the Worker Adjustment and Restraining Notification Act ("WARN Act"), 29 U.S.C. §§ 2101-2109, applied to the debtor, United Healthcare System, Inc. ("Debtor"); and it appearing that this Court has jurisdiction over this appeal pursuant to 28 U.S.C. § 158(a); and it further appearing that a district court reviews a bankruptcy court's opinions under a clearly erroneous standard for findings of fact and under a *de novo* standard for conclusions of law. *See* Fed. R. Bankr. P. 8013; *Donaldson v. Bernstein*, 104 F.3d 547, 551 (3d Cir. 1997); and it further appearing that by late 1996, the Debtor was aware of the gravity of its financial difficulties such that

Debtor ceased paying its premiums for employee health insurance and subsequently diverted employee paycheck deductions for health insurance, savings bonds, retirement benefits, credit union loans and court ordered child support and alimony payments for its own business purposes; and it appearing that the Debtor's financial problems were sizable, long-term and critical; and it further appearing that the Debtor's Board of Trustees recognized that merely refinancing or acquiring new lenders would not prevent the closing of the hospital; and it further appearing that neither the unforeseeable business circumstances exception, 29 U.S.C. § 2102(b)(2)(A), nor the faltering business exception, 29 U.S.C. § 2102(b)(1), apply to exempt the Debtor from liability under the WARN Act; and it further appearing that actual necessary costs and expenses of preserving an estate, including wages for those services rendered following the bankruptcy filing, are entitled to classification as first priority administrative claims. *See In re Hanlin Group, Inc.*, 176 B.R. 329, 332 (Bankr. D.N.J. 1995) (citing 11 U.S.C. § 507(a)(1) and 11 U.S.C. § 503(b)(1)(A)); and it further appearing that the Debtor requested that 1,300 employees report to work for 16 days after the Debtor's bankruptcy filing on February 19, 1997; and it further appearing that these employees performed necessary and valuable services to the estate; and it further appearing that the Debtor was an employer for 16 days after the bankruptcy filing; and it further appearing that the Debtor's Board of Trustees in exercising its business judgment acted properly in notifying the employees of the bankruptcy filing and subsequent closing pursuant to the WARN Act; and it further appearing that the agreement between the Debtor and St. Barnabas Health Care System

stipulated that the Debtor would give notice to the Debtor's employees pursuant to the WARN Act; and the Court having conducted a *de novo* review of (1) the underlying record; (2) the relevant Opinion and Order; and (3) the submissions of the parties; and good cause appearing;

IT IS on this 5th day of November, 1998,

ORDERED that Appellant's appeal of the March 26, 1997 Opinion and Order of the States Bankruptcy Court, District of New Jersey (Tuohey, J.), is hereby DENIED;

IT IS FURTHER ORDERED that the March 26, 1997 Opinion and Order of the United States Bankruptcy Court, District of New Jersey (Tuohey, J.), is hereby AFFIRMED; and

IT IS FURTHER ORDERED that a copy of this Order be served on all parties within seven (7) days of the date of this Order.

s/ Joseph A. Greenaway, Jr.
JOSEPH A. GREENAWAY, JR.,
U.S.D.J.

APPENDIX C — OPINION AND ORDER OF THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF NEW JERSEY DATED AND FILED MARCH 5, 1997

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW JERSEY

Case No. 97-21785(WFT)

Chapter 11

Hearings: February 27, 28;
March 4, 5, 1997

In Re:

United Healthcare Systems, Inc.

Debtor.

* * *

OPINION

TUOHEY, WILLIAM F.

The within debtor filed a Chapter 11 bankruptcy petition at 12:36 PM on Wednesday, February 19, 1997. On the same date, said debtor also filed an Order Shortening Time requesting the Court to schedule a hearing on short notice for the sale of certain good will and trade names of the debtor. The Court scheduled said hearing for February 27, 1997,

and the hearing commenced on said date.[1] The Court further notes that the sale of assets pursuant to Bankruptcy Code §363 as sought by the debtor is a "core" proceeding as defined by the Federal Congress in 28 U.S.C. §157.

FINDINGS OF FACT

United Healthcare Systems, Inc. ("United" or "debtor") is a non-profit corporation of the State of New Jersey. The debtor operated the Children's Hospital of New Jersey at Ninth Street in Newark, New Jersey, and further operated an entity known as United Hospitals Medical Center also in Newark as well as clinic facilities. Prior to filing bankruptcy, the debtor employed approximately 1,200 employees and as of the date of the filing of the bankruptcy had approximately 165 patients in its facilities[2] for which it was providing medical care.

The New Jersey Legislature in 1985 passed a statute entitled "Children's Hospital of New Jersey designation as the State's specialty acute care children's hospital for northern New Jersey." *N.J.S.A.* 26:2H-18(a), the statute provides:

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1. The hearings continued for four days and the Court heard the testimony of five witnesses.

2. Seventy patients were infants, the balance adults. By noon, Friday, February 20, 1997, all of debtor's patients were either discharged to home or transferred to other institutions pursuant to their families' and their treating physicians' direction (Testimony of Mr. Ostrowski).

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"The Commissioner of Health shall designate Children's Hospital of New Jersey, a unit of United Hospitals Medical Center, as the State's specialty acute care children's hospital for northern New Jersey."

The legislative history at the time the statute was adopted in 1985 notes the following:

"Children's Hospital of New Jersey, a unit of United Hospitals Medical Center in Newark, New Jersey, is the only acute care facility in the State that is committed exclusively to the provision of diagnostic and specialty treatment services for children and is the major pediatric training facility for medical students from the University of Medicine and Dentistry of New Jersey.

The children treated at the Children's Hospital of New Jersey tend to be the most severely ill children in the State and are often referred to the hospital from other facilities when those facilities are unable to provide the needed specialized or critical care a child needs and consequently the case mix at Children's Hospital of New Jersey is unique in the State.

The comprehensive array of specialized healthcare services provided at Children's Hospital of New Jersey, the intensity needed by seriously ill children and the subsequent longer lengths of stay serve to differentiate Children's

> Hospital of New Jersey from other acute care hospitals in the State.
>
> It is in the best interest of the children of New Jersey that the State designate and support an acute care specialty hospital which is dedicated exclusively to the care of children."

Initially, the Newark facility was the only dedicated children's hospital within the State of New Jersey. The Legislature in 1987 designated Cooper Hospital/University Medical Center as the designated specialty acute care children's hospital for southern New Jersey (*N.J.S.A.* 26:2H-18(c)). In 1992, the State designated Robert Wood Johnson University Hospital as the specialty acute care children's hospital for central New Jersey (*N.J.S.A.* 26:2H-18(d)); and finally, in 1993, the State designated St. Joseph's Hospital in Paterson, New Jersey as the specialty acute care children's hospital for certain counties in northern New Jersey (*N.J.S.A.* 26:2H-18(e)). Thus, the debtor is one of four statutorily designated special facilities dedicated to providing acute care medical services to children.[3]

The unique function of the debtor's hospital services located within Essex County, New Jersey, is highlighted by an affidavit submitted to the Court by the Commissioner of Health and Senior Services for the State of New Jersey, Len Fishman:

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3. Included in the certificates of need held by debtor is the right to perform pediatric cardiac surgery on newborns. Only two other institutions in New Jersey hold said privileges.

Appendix C

"It was particularly important that these services be available to families of the City of Newark, County of Essex, State of New Jersey and the surrounding areas because of existing medical and social conditions in that service area. Many children live in poverty, are of low birth weight and are at high risk for infant mortality which necessitates immediate and timely intervention. In order to ensure such medical help the New Jersey Legislature determined it was best to be undertaken by a comprehensive children's hospital in that community.

United functioned in this role for several years. United brought together in one location, a critical mass, as stated, of vital pediatric service. These services are crucial and enabled physicians to develop their expertise in this area. Such a grouping facilitates the development of a residency program and academic affiliation. (¶s 5 and 6 of Fishman Affidavit filed February 26, 1997).

The Commissioner further states in his Affidavit that on or about January 16, 1997, United advised the Commissioner and his staff that it was experiencing serious financial difficulties. On January 27, 1997, the Department of Health and Senior Services placed its own inspectors on the site of United so as to continuously monitor conditions while United continued to seek help for its economic crisis.

Appendix C

On January 29, 1997, the State of New Jersey retained a financial advisory firm by the name of Alex Brown & Sons, which specialized, among other things, in the sale and merger of institutions involved in the healthcare industry. The Commissioner advises us in ¶12 of his Affidavit that Alex Brown was retained in order to assist the State in facilitating an orderly process that would preserve in Newark the critical services provided at United.

For its part, the Board of Trustees ("Board") of the debtor retained Cain Brothers & Company, Inc. ("Cain") an investment banking institution to aid it in its search for a financial solution to the hospital's problems. Mr. Thomas Barry, Vice President of Cain, testified before the Court on February 27 and 28, and March 4, 1997. Mr. Barry confirmed that his firm was retained on February 1, 1997 and that his first observations were that the institution was in financial extremis. The bed census was deteriorating; the staff was at a low morale and physicians were preparing to leave the hospital. Mr. Barry further testified that in his opinion the institution was "effectively insolvent." As a first interim step through Cain, Mr. Barry recommended to the trustees that a new management team be brought in to hold the institution together for the short term. An organization referred to as "Quorum" became the chief operating entity of the debtor and the Quorum personnel reported directly to the Board.

Commissioner Fishman in ¶13 of his Affidavit advises that in late January 1997, the Commissioner became aware of the fact that other medical institutions were contacting the debtor's medical staff in order to make employment arrangements with various members of the medical staff.

Commissioner Fishman perceived this as being detrimental to the goal of maintaining a high quality children's hospital in Newark because it would have lead to the doctors essentially being "picked off" by the various institutions competing for the staff. The Commissioner also states in ¶13 that he felt that if this process was not stopped immediately that only a "carcass" with a dissipated critical mass of health services would remain and that this was against the public good. With this in mind, the Commissioner advises that on January 30, 1997 his staff contacted the chief executive offices at St. Barnabas Healthcare System ("St. Barnabas"), University of Medicine and Dentistry of New Jersey ("UMDNJ"), Cathedral Healthcare Systems ("Cathedral"), Primary Health Systems of Pennsylvania ("Primary") and St. Joseph's Hospital and Medical Center ("St. Joseph's") and requested that said institutions accept a two-week moratorium on negotiating with the medical staff at United. The said institutions abided by the Commissioner's request and commencing January 30, 1997 agreed that no solicitation of medical staff would occur for a two-week period.

Mr. Barry advised the Court that it soon became apparent that the debtor must either merge with another institution or sell its good will and operation to another institution. Mr. Barry further advised the Court that by early February he had determined that the debtor was losing $3.5 million each month and that the debtor's cash needs were approximately $10 million per month. The debtor in consultation with the Board and its professionals prepared a request for proposals ("RFP") on or about February 4, 1997 (Exhibit D-1, Tab 1). The so-called RFPs were sent to all institutions that expressed an interest in the United facility and requested that they file

a response by February 10, 1997. Mr. Barry testified that this was one of the fastest RFPs he had ever worked on and that the extremely tight timetable was necessitated by the fact that the debtor was quite simply out of cash and was unable to purchase needed supplies such as blood etc.

The RFP advised prospective parties that their proposals were to be submitted by February 10, 1997 and that it was the goal of the hospital to have a definitive agreement executed by February 24, 1997 (RFP at page 9).

In response to the RFP request, an entity referred to as "PHS" on February 13, 1997, submitted a proposal (Exh. D-1, Tab 6). On February 15, 1997, Primary submitted its proposal (Exh. D-1, Tab 7). On or about February 14, 1997, UMDNJ in conjunction with Cathedral submitted a joint response to the RFP (Exh. D-1, Tab 10; as modified by Tabs 8, 9 and 13). St. Barnabas submitted its proposal on February 16, 1997 (Exh. D-1, Tab 11).[4]

Mr. Barry, in his testimony, advised the Court that in all, five parties responded in some form to the RFP. Four formal RFP's were submitted. Each proposal was submitted to the State through Alex Brown. Mr. Barry testified that on February 11, 1997, the Board met with three applicants — St. Barnabas, UMDNJ/Cathedral, and the Primary group out of Jersey City. A fourth entity referred to as the "Chicago Group" met with the Board on February 12, 1997. The Court was further advised by the testimony of Mr. Barry that the aforesaid four bidders who had expressed serious interest

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4. The final agreement between debtor and St. Barnabas is contained in Exh. D-1, Tab 15.

on Thursday, February 13, 1997 at 3 PM all participated in a conference call with the office of the Commissioner of Health dealing with their responses to the RFP and the issues involved in a certificate of need application. Mr. Barry testified that this conference call with all parties, the Department of Health, and the debtor lasted one and one-half hours.

Mr. Barry in his testimony (February 27, 1997) advised the Court that all parties including the Commissioner of Health were anxious to have a final decision on acceptance or rejection of an RFP proposal by the weekend commencing Friday, February 14, 1997. This was a critical date because this was the date fixed for the expiration of the two-week moratorium on seeking to employ debtor's physician staff. To this end, on Sunday, February 16, 1997, commencing at 5:30 PM there was a meeting of the medical staff and the Board of the debtor in a joint session involving approximately 100 people. Starting at 6 PM, the then three remaining applicants — UMDNJ/Cathedral, St. Barnabas and Primary — each in turn made an oral presentation of approximately thirty minutes. Through various caucuses and meetings on the evening of Sunday, February 16, 1997, Mr. Barry advised us that by 10 PM, Primary was no longer treated as a bidder. Thus, by 10 PM, Sunday, February 16, 1997, the Board was faced with two viable responses to the RFP — St. Barnabas and UMDNJ/Cathedral.

Commissioner Fishman in ¶24 of his Affidavit advises the Court that on February 13 and 14, 1997, the State sent representatives to the two St. Barnabas facilities involved in their proposal as well as to the UMDNJ/Cathedral facilities

and Primary's to commence the necessary due diligence by the Commissioner of Health from a "regulatory perspective."

Commissioner Fishman spoke to the debtor's Board on a speaker phone on Sunday, February 16, 1997 outlining the Commissioner's concerns as to each bid before the Board but remaining impartial in providing the analysis to the Board (Fishman Affidavit, ¶26). The Commissioner in his Affidavit further advises that there was no representative of the State of New Jersey present in the meeting of the Board when the Board debated and decided the issue of its selection of a successful bidder. However, while no one sat in on the Board meeting, Mr. Barry has testified that throughout Sunday evening, February 16, 1997, representatives of the State particularly staff from Alex Brown were down the hall and were kept apprised of all that was transpiring during the course of the evening.

Mr. Barry and the other witnesses all agreed that neither UMDNJ/Cathedral or St. Barnabas saw or were aware of the amount of each other's proposal. Mr. Barry testified he was meticulous in instructing the Board to have contact with any bidder, that all negotiations were through him and that no bidder was to know the amount of the other side's proposal. Thus, through the voting by the Board, there was no opportunity for either side to increase their offer. The Board was faced with accepting one proposal or the other.

The Court finds it was the clear intention of the parties that after a contract was signed on February 17 or 18, 1997, that the bankruptcy would be filed on February 19, 1997 and in the §363 bankruptcy process the Court would have

the opportunity to take higher and better offers, subject to the Commissioner's approval required in the certificate of need process. The Court comes to this conclusion from the testimony of the witnesses and the RFP, as well as Exh. D-3 in evidence and the Order to Show Cause filed on the first day of the bankruptcy which asks the Court to hold a §363 sale and requests a so-called "break-up fee" for St. Barnabas in the event it is outbid before the Bankruptcy Court.[5]

In his testimony before the Court (February 27, 1997), Mr. Barry advised that the Board voted by secret ballot and that the first vote was taken at 1 AM on February 17, 1997. When the first ballots were opened and counted, the vote was 9 in favor of the UMDNJ/Cathedral plan and 6 in favor of the St. Barnabas plan. Mr. Barry states that immediately after this vote was taken, corporate counsel for the debtor, Mr. Jeff Becker advised the Board that since the bulk of the assets of the debtor were being sold, it was his opinion that pursuant to state law, the vote of the Board should be by "super majority." It is stated that Mr. Becker left the meeting at 1 AM and returned to his law office to verify said information and telephoned the Board that yes his understanding was correct, a super majority vote would be required. Approximately twenty minutes after the aforesaid first vote, a second secret ballot was taken. This second secret ballot resulted in ten votes for the St. Barnabas plan and five votes for the UMDNJ/Cathedral plan. Mr. Barry stated that the time frame between the two votes was approximately twenty minutes.

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5. The St. Barnabas contract (Exh. D-1, Tab 15) expressly recognizes that in the bankruptcy process, St. Barnabas might be outbid.

Appendix C

At 8 AM, Monday morning, February 17, 1997, there was a two and one-half hour conference call involving approximately 35 people. It is the testimony of Mr. Barry that approximately ten to fifteen participants in the call represented various state agencies and officials from New Jersey including the Governor's office and the Commissioner's office. The rest of the people who participated in the Monday morning telephone conference call were from the debtor and its professional personnel. None of the bidders participated in the 8 AM Monday morning, February 17, 1997 conference call.

Mr. Barry further testified that all bidders prior to the vote on February 16, 1997 had been advised that the timetable of the Board required that once the Board had selected a successful bidder that said party would have until approximately 9 PM on Monday, February 17, 1997 to negotiate a written agreement in conformance with the RFP proposal. It was understood by all parties according to the testimony of Mr. Barry that if a written agreement was not executed by the evening of February 17, 1997 the process would be reopened and the unsuccessful bidder would be allowed to reenter the process. Mr. Barry testified that while no written agreement was signed with St. Barnabas, by the evening of February 17, he stated that a firm agreement had been reached and that a handshake with St. Barnabas' group had been achieved and that the written contract memorializing that agreement was signed the following day, February 18, 1997. The Court finds the parties intended to present this agreement to the Bankruptcy Court as the detailed agreement against which higher bids would be entertained in the §363 sale process. On said date, a joint

letter signed by the debtor and St. Barnabas was faxed to the Department of Health and requested that in order to implement the proposal with St. Barnabas, Commissioner Fishman should issue "Certificates of Need" to the St. Barnabas group and further terminate the certificates of need of the debtor. This February 18, 1997 fax also confirms that the debtor planned to file bankruptcy on Wednesday, February 19, 1997 (Exh. D-1, Tab 18).

Based upon the testimony of both Messrs. Ostrowski and Barry, the Court finds that the parties understood, based on the February 13, 1997 telephone conference between all bidders and the Commissioner's staff, that while the certificate of need request would be expedited, it would take several days during which the higher or better offering process in bankruptcy could proceed.

Approximately six hours after receipt of the debtor's and St. Barnabas fax, Commissioner Fishman issued his reply in a return fax granting the requests of the debtor and incorporating certain findings of the Commissioner (Exh. D-1, Tab 19).

COMPARISON OF TWO PROPOSALS

Cain, under the supervision of Mr. Barry, prepared a comparative analysis of the St. Barnabas and UMDNJ/ Cathedral RFPs. This analysis in written form was presented to the Board prior to their February 16, 1997 vote. A copy of the analysis has been placed in evidence as Exh. D-3 before the Court.

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Under both proposals, the hospital's land and buildings remain in the bankruptcy estate and are not acquired by either applicant. Virtually, all beds, furniture and fixtures, subject to liens and leases, also remain with the debtor and are not part of the acquisition. Exhibit D-3 also summarizes that all sides understood that the sale process would be consummated with a bankruptcy code §363 hearing. In this respect, Exh. D-3 on page 2, on analyzing the St. Barnabas and the UMDNJ/Cathedral plans under the heading "Form of Transaction" states for both applicants "bankruptcy filing and purchase of assets." Mr. Barry testified that prior to voting, the Board was advised through Exh. D-3 as well as a lengthy presentation he made to the Board over a two hour period prior to voting, that the St. Barnabas proposal was for $13 million in cash and the UMDNJ/Cathedral proposal was for $12 million in cash but the UMDNJ/Cathedral proposal also included a waiver of $1.2 million in accrued liabilities owed by the debtor to UMDNJ. Mr. Barry further stated that one of the primary concerns of the Board was the job security for as many employees as possible as well as the issue of staff privileges for the medical faculty. In regard to these issues, Mr. Barry stated that the Board was advised that as of the time of the voting, St. Barnabas agreed to hire 275 employees and UMDNJ/Cathedral would hire 175 immediately and by ten days after closing UMDNJ/Cathedral committed to employ 560 of debtor's former employees.

Exhibit D-3 and the testimony of Mr. Barry further confirms that the Board was advised that the salaried physicians currently employed by the debtor would be given comparable contracts at St. Barnabas for at least six months. UMDNJ/Cathedral agreed to retain all such doctors for a one-year period.

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By the time the vote was taken, both RFP proposals stated that the closing would occur within two or three days of the vote by the Board, that all assets other than the good will would remain with the debtor, and that none of the debtor's liabilities would be acquired by either institution. Mr. Barry stated that he viewed his role as a fact finder on behalf of the Board and that as such, he simply presented the details of each plan to the Board and made no recommendation to the Board on their choice of an institution.

Commissioner Fishman's Affidavit also indicates that in his telephone conference call to the Board on the night of February 16, 1997, he did not favor one of the two remaining proposals over the other and left the choice to the Board.

At the Court hearing (February 28, 1997) on the record in the Bankruptcy Court proceeding, St. Barnabas increased its offer for the debtor's assets that are currently being sold to $14 million with an additional formula that if 1997 charity care reimbursement to St. Barnabas increases by over $1 million, there is a participation by the debtor pursuant to a formula placed on the record. On March 4, 1997, UMDNJ/ Cathedral stated on the record they would increase their offer to $18 million. Thus, $5 million higher than the proposal the Board voted to accept.

BANKRUPTCY CODE §363

The fundamental test that a Bankruptcy Court must look to in approving a bankruptcy code §363 sale is whether or not the proposed transaction is put forth in good faith and

whether the sale is for a fair value. This test was set forth in *In Re Abbott Dairy*, 788 F.2d 143 (3rd Cir. 1986). One of the Circuits has noted that the primary function of the bankruptcy court is to determine whether or not there is sound business reason to justify the proposed sale. *Continental Airlines, Inc.*, 780 F.2d 1223 (5th Cir. 1986).

The test in the Second Circuit is set forth in *In Re Lionel Corp.*, 722 F.2d 1063 (2nd Cir. 1983). The Court held that there must be some articulated business justification to move forward with the transaction. Circuit Judge Cardamone in writing the *Lionel* Opinion had occasion to note at page 1069:

> "[2] First and foremost is the notion that a bankruptcy judge must not be shackled with unnecessarily rigid rules when exercising the undoubtedly broad administrative power granted him under the Code. As Justice Holmes once said in a different context, '[s]ome play must be allowed for the joints of the machine. . . .' Missouri, *Kansas & Texas Ry. Co. v. May*, 194 U.S. 267, 270, 24 S.Ct. 638, 639, 48 L.Ed. 971 (1904). To further the proposes of Chapter 11 reorganization, a bankruptcy judge must have substantial freedom to tailor his orders to meet differing circumstances. This is exactly the result a liberal reading of §363(b) will achieve."

Circuit Judge Colin Seitz in the Third Circuit *Abbott* Opinion had occasion to note at page 147:

> "Unfortunately, neither the Bankruptcy Code nor the Bankruptcy Rules attempts to define 'good

> faith.' Courts applying section 363(m) and its predecessor, Fed.R.Bankr.P. 805) have, therefore, turned to traditional equitable principles, holding that the phrase encompasses one who purchase in 'good faith' and for 'value.' *See, e.g., In re BelAir Assocs.*, 706 F.2d 301, 305 (10th Cir. 1983); *In re Rock Indus. Mach. Corp.*, 572 F.2d 1195, 1197 (7th Cir. 1978)."

The Court has also considered the case *In Re Country Manor of Kenton, Inc.*, 172 B.R. 217 (Bankr.N.D. Ohio 1994). Bankruptcy Judge Speer in this case wherein he had to review the sale of a nursing home license and other assets in connection with the operation of a nursing home noted that the Sixth Circuit in which he sat adopted the *Lionel* test, *supra*. In *Kenton*, the bankruptcy court went on to state at page 220:

> "[2][3] The sound business purpose test has four (4) requirements: 1) sound business reason; 2) accurate and reasonable notice; 3) adequate price; and 4) good faith. *In re Plabell Rubber Products, Inc.*, 149 B.R. 475 at 479 (Bankr.N.D. Ohio 1992)."

Put simply, the fundamental question the Court must ask is, has the Board of Trustees in the within matter exercised sound business reasons and judgment in exercising its prerogative to accept the St. Barnabas offer and, has a fair and reasonable price been achieved. Mr. Barry, in testifying for the debtor, stated that his presentation to the Board as their consultant advised them that they had four areas with

which they must concern themselves. Mr. Barry advised the Board that they should consider the plan that was in the best interests of the patients; the best interests of the employees; the plan that most fairly treated the issue of employment and privileges for physicians, and finally, they should consider which plan was financially most cogent. When this four-prong test of business judgment is applied to the voting of the Board, their business judgment is found lacking by this Court. The Court finds the UMDNJ/Cathedral proposal saved more jobs; gave better protection to physician contracts and was for more money when the waiver of UMDNJ's over $1 million claim is factored in the equation. Further, the Court concludes the price is not adequate based upon the $5 million higher offer on the record as of March 4, 1997.

If the debtor had not operated a critical care medical facility and the sole issue was the business judgment test springing from *Abbott* and *Lionel*, this Court would not hesitate to state that the creditors should not be bound by the business judgment of the Board at the Sunday, February 16, 1997 meeting and that the process should be reopened and a full and complete auction hearing pursuant to the provisions of bankruptcy code §363 should be held. However, the debtor is a critical care hospital institution and its operations by statute and administrative code of the State of New Jersey are under the jurisdiction of the Commissioner of Health.

The Court has reviewed in detail the Affidavit of Commissioner Fishman and has further reviewed in detail his administrative findings and holdings as set forth in his February 18, 1997 letter to the debtor and St. Barnabas (Exh. D-1, Tab 19).

Appendix C

The Court particularly notes the language of Commissioner Fishman on page 4 of his opinion to the parties:

> "In analyzing this application, I begin with the fact that United has been a children's hospital, providing these services to the children of Newark, Essex County, and the entire State for many years. During this period, United has brought together in one location a critical mass of vital pediatric services. This critical mass of services is crucial in enabling physicians to develop and maintain expertise in this area. Having these services grouped in this fashion supports many subspecialties of services, the development of a residency program and academic affiliations. If I fail to take action now, on an expedited basis, I believe that there will be a dispersal of these critical services. It is therefore essential that I ensure that these services continue to be consolidated and provided to the City of Newark. Accessibility to services by the families of Newark and the surrounding area is necessary because of the existing medical and social conditions. Many children live in poverty, are low birth weight, and at high risk for infant mortality, which necessitates timely intervention best undertaken by a comprehensive children's hospital in their community."

The Court finds the submission to the Commissioner on February 18, 1997 of the joint application of St. Barnabas

and the debtor (Exh. D-1, Tab 18) which sought to terminate the debtor's certificates of need and issue new ones to the St. Barnabas group was a nullity. This request violated the intent of the parties as set forth in the RFP and the testimony before this Court. The Board and its agents' actions in seeking to terminate the certificates of need of the debtor twenty-four hours before filing bankruptcy caused a valuable asset of the estate to be placed in jeopardy. This action has defeated the ability of this Court to carry out its function to obtain a fair price for the debtor's assets for the benefit of the creditors of this estate. Because said actions of the Board, taken under the advice of its hired consultants and transaction counsel was taken at a time when the bankruptcy filing was hours away and because said action deprived the Court of its ability to receive higher and better offers, this Court finds the request to terminate the debtor's certificates of need prior to the Bankruptcy Court's review was void and a nullity. If the debtor was concerned about its patients as it well should be, the Commissioner could have been asked to take temporary emergent action to achieve the purpose of protecting the patients and aiding in their transfer to another institution and still yet preserve the debtor's greatest asset — its good will connected to its certificates of need.

None of the aforesaid appears to have been presented to the Commissioner by the debtor or St. Barnabas. The Commissioner was faced with a scenario where he had to act immediately to preserve the integrity of the care of the debtor's patients. The Court finds that the Commissioner was not advised that it had been the intent of the parties throughout the RFP process to hold an emergent hearing in

the Bankruptcy Court so that higher and better offers could be entertained with the express understanding that said higher and better offers and the issuance of certificates of need necessary to implement them would be submitted to the Commissioner so that he could exercise his jurisdiction of approving all certificates of need.

This Court finds the request to void debtor's certificate of need on the eve of bankruptcy violated the federal statutes and under Bankruptcy Code §105 the debtor is directed to petition the Commissioner to reconsider his February 18, 1997 findings; and to reinstate the debtor's certificate of need for a ten-day limited period for the sole purpose of allowing the Bankruptcy Court to carry out its bankruptcy functions under Bankruptcy Code §363. At the conclusion of the §363 process the matter will be returned to the Commissioner to review and approve or reject the qualifications of the highest bidder and their ability to hold the certificates of need required.

Thus, for all of the aforesaid reasons, the request of the debtor and St. Barnabas to approve the actions of the Board in granting and entering into the contract with St. Barnabas is denied at this time. This Court retains jurisdiction for the purpose of holding a §363 sale and further retains jurisdiction should the Commissioner fail to reopen this process to determine the status of the pending St. Barnabas offer. All monies on deposit and all rights of the parties are preserved pending the debtor's application to the Commissioner for reconsideration in accordance with the Opinion set forth herein. Should the Commissioner not reconsider, the debtor's

and Committee's right to request this Court to accept the $14 million St. Barnabas proposal is preserved.

DATED: March 5, 1997

s/ William F. Tuohey
HONORABLE WILLIAM F. TUOHEY
U.S. Bankruptcy Judge for the Federal
District of New Jersey

Appendix C

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW JERSEY

Case No. 97-21785(WFT)

Chapter 11

Hearings: February 27, 28;
March 4, 5, 1997

In Re:

United Healthcare Systems, Inc.

Debtor.

ORDER

This matter having come before the Court wherein the debtor and St. Barnabas seek this Court's approval pursuant to Bankruptcy Code §363 of a sale of certain good will assets of the debtor to St. Barnabas; and this Court having conducted hearings over several days and the Court having rendered its written findings in an Opinion this date, the terms of which are incorporated herein;

IT IS on this 5th day of March, 1997

ORDERED that the application of the debtor seeking, pursuant to Bankruptcy Code §363, approval of the Court of a sale to St. Barnabas of certain assets is denied at this time pending the debtor taking the actions set forth in this Court's

written Opinion entered this date. The Court expressly reserves jurisdiction on the St. Barnabas offer and the Court further reserves jurisdiction on the sale of debtor's assets.

s/ William F. Tuohey
HONORABLE WILLIAM F. TUOHEY
U.S. Bankruptcy Judge for the Federal
District of New Jersey